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REFORMING INTERNATIONAL FINANCIAL INSTITUTIONS

The Bretton Woods Institutions were created more than fifty years ago. At the time, their object was to manage the international payments system and to assist in the reconstruction of Europe. The world has changed since then. A recent study prepared by the World Institute for Development Economics Research of the United Nations University, points out the urgent need to reform the International Monetary Fund and the World Bank. How can these changes be brought about? In this edition of **World Chronicle**, John Langmore, Director of the Division for Social Policy and Development of the United Nations' Department of Economic and Social Affairs, talks about the globalization of the economy and the changes that this process may bring to UN institutions.

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ANNOUNCER: From United Nations Headquarters in New York, this is **World Chronicle**, an unedited interview programme about major global issues.

Here now to introduce our guest is the host of today's **World Chronicle**.

LITTLEJOHNS: I'm Michael Littlejohns, and this is **World Chronicle**.

A major new study called "New Roles and Functions for the United Nations and the Bretton Woods Institutions", calls for urgent change within the United Nations system. The study has been prepared by the World Institute for Development Economics Research of the UN University, with support from the UN's Department of Economic and Social Affairs. This wide-ranging document states that the UN, the World Bank and the International Monetary Fund are operating on outdated political and economic foundations. They need to be overhauled before a crisis induced by globalization forces the changes required. The document also calls for repealing the Security Council veto accorded to the five major post-war powers in the 1940's and the addition of other countries as permanent members of that body. But can these far reaching changes be implemented?

Our guest today is the Director of the Division for Social Policy and Development at the United Nations Department of Economic and Social Affairs, John Langmore. Joining me to talk with Mr. Langmore are Robert Holloway of *Agence France-Presse/AFP* and Linda Fasulo of *NBC News*.

Mr. Langmore, welcome to **World Chronicle**.

LANGMORE: Thank you.

LITTLEJOHNS: Mr. Langmore, I think it's going to be a cold day in hell when the veto of the Security Council is cancelled. You know what a terrible process would be involved in getting that done so I think we can write that one off. Now as far as the ...

HOLLOWAY: You want to talk about that?

LITTLEJOHNS: Now, wait a minute. Wait a minute. As far as the Bretton Woods institutions as they're called are concerned, because they emerged from a place called Bretton Woods in New Hampshire -- the World Bank and the International Monetary Fund can far-reaching changes be implemented there? I mean this is more your territory than canceling the veto of the Security Council. So let's talk a bit about the possibility of implementing changes in those institutions, particularly in light of certain statements that

have been made by the new administration in the United States. Perhaps the prospects for change, reform, improvement, whatever, in those two institutions and bringing the UN more into the economic matters has improved?

LANGMORE: It depends what member countries want. I mean if the member countries are dissatisfied with the performance of the Bank and the Fund now -- and there is some reason for that dissatisfaction on various grounds -- then they'll push for reform. And given that the world is becoming a more interdependent place, and no one would dispute that, and given the fact that the countries have to cooperate much more effectively to achieve economic development targets of the kind that they want, and given the fact that the Fund and the Bank have not been as successful as they would like to have been, it raises the questions about whether they are adequately governed, whether their policies have been correct, and so on. And most developing countries – and it could well be all -- are dissatisfied with the level of influence they have within the Bank and the Fund, which really the donor countries have control of the Fund particularly, but also to a large extent the Bank, and the borrowing countries, which provide the income for the Bank and the Fund. Now, that's clearly unfair and given that the developing countries don't really have nearly as much say about what the policies should be. There also have been, I think it's true to say, a global reaction against the very narrowly focused Washington consensus and that grew out of to some extent the structure, or the way that Bank and Fund are organized. The Bank at least would say that we're now working in a post-Washington consensus style, a much more consultative one; much more concerned about poverty and equity and the spread of economic development broadly. The Fund hasn't changed nearly as much but it's under pressure to change because it didn't cope particularly well with the financial crises of 1997 and 1998. So there are lots of reasons why you could expect there would be pressure for change. You could also expect pressure from change from the Bush administration. Republicans in Congress commissioned the report on the Fund and Bank last year which argued for a contraction in their role. A sharper focus in their role.

LITTLEJOHNS: That's not what you guys want?

LANGMORE: Well, we want both an expansion and a contraction. We want less conditionality, so contraction in the...

LITTLEJOHNS: But how can you avoid conditionality? If you go to the bank, or I go to the bank, anyone around this table goes to the bank, there are certain things – I mean to borrow money, not to put it in, to borrow money -- there are certain conditions that you have to meet. So why is this unfair for the Bretton Woods institutions, particularly the World Bank, to impose conditions on borrowers?

LANGMORE: Some level of conditionality is obviously essential because that's necessary to ensure that loans are honestly and efficiently used.

LITTLEJOHNS: Which, in many cases, they are not. There is so much corruption. Come on, let's face it.

LANGMORE: They're not as efficiently used as they should be in some cases. I can't tell you what proportion of the cases but in many cases they are very efficiently used and in those cases why should the Bank and Fund require 300 different conditions about the ways those should used? Why not recognize that part of development is political development, the capacity to make decisions within the development countries themselves so that they own and take control of the funds at their disposal and learn to use them efficiently in their own ways. It's not necessary to tell most developing countries that they should be building up their expenditure on basic education. They know that. They want to do it ..

FASULO: So why aren't they doing it?

LANGMORE: Many are. Many are and some aren't doing it as much as they should, but many are and many will do it more if the funds were available.

LITTLEJOHNS: Health services, are they doing anything? Very little in the way of health services.

LANGMORE: It varies enormously Michael. It's very difficult to make the very broad generalizations. Some countries are not spending nearly enough on health services because they're spending too much on defense. That's true. But others are spending as much as they possibly can and very, very little on defense. You can't make absolute generalizations, I don't think.

FASULO: So what would be wrong with the World Bank exerting some kind of pressure on governments to do the right thing for their people? You know, governments that are spending a disproportionate share of their funds on defense for their own self-interest

rather than on education and health for their people. What's wrong with the World Bank saying this is what should be done if you want this money?

LANGMORE: It's a question of tailoring the conditions to each country's circumstance and that might be appropriate in certain cases where inefficiency and corruption and misjudgment are pretty clearly present. But is it necessary all the time? I wouldn't have thought so and the Bank and the Fund have been far too assertive and far too comprehensive in the kinds of conditions that they have imposed. And most developing countries are very critical of that and say we would like to develop politically. I mean it's almost neo-colonial to be treated in the way the Bank and the Fund often do treat countries. So to give more freedom to them to manage their own affairs, as the Bank now says it wants to do, seems highly desirable as far as that's possible.

HOLLOWAY: If you could perhaps spell out the reforms that you would like to see. The question I wanted to ask you concerns the relevance of these two institutions. One of the major changes that has taken place in recent years is a shift from development assistance to direct private investment in developing countries. Does that shift and the fact that private investment now eclipses all other kinds of capital flows as far as I'm aware, does that mean that these countries can be much more resistant if you like to the kind of pressure that the Bank and the Fund have been putting on them so far?

LANGMORE: Foreign direct investment is a great benefit to a small number of countries -- to China and about dozen others -- but most of Africa and many parts of Asia, and even some of Latin America don't receive very much from direct foreign investment unless it's in purchasing privatized enterprises. One very interesting figure, which is not quite answering your question but it's very important to acknowledge, is that of global financial flows in investment about two-thirds goes to the United States. Only a third goes to all the rest of the world. And you can imagine how much of that third goes to developing countries and to countries with economies in transition and given that most of that does go to that group – goes to China and a few other places – there's next to nothing. I mean last year nine billion went to the whole of Africa.

HOLLOWAY: So we shouldn't see this as substitute a for development assistance?

LANGMORE: No, no -- it's entirely desirable. One wants to encourage it and to create the conditions where it's possible and as effective as it can be but it's not an answer for many of the really poor countries. So they need aid, they need loans through the Bank and Fund because there is no other source to get these funds except from bilateral arrangements with donors.

HOLLOWAY: Apart from reforming the voting structure within these two organizations, what other reforms would you like to see, or what other reforms does the report advocate?

LANGMORE: I think one of the principal reforms is in the nature of the policies advocated by those institutions. They have been dominated by what's called "the Washington consensus" which means liberalizing everything, privatizing, cutting back on government and so on. And I think that there's a recognition that that liberalization went too far too fast, and without adequate preparation, and that there needs to be a much better consideration of the different circumstances of each country and strategies designed that suit those countries so that they don't liberalize their financial markets for example until they have a strongly developed institutional framework for managing finance within the country itself. Otherwise, it's a recipe for financial breakdown in a way that we've seen it too commonly in countries, in economies in transition. It's that kind of not one model fits all but recognizing the differences that, I think, is one of the principal reforms required. Now the Bank would say they're doing that, and I'm sure that they are to some extent, but there's quite commonly a difference between what the Bank says it's doing and what it actually does on the ground. And there's a need to apply what its aspirations are to what it actually does much more rigorously. The Fund hasn't changed nearly as much. It's still, on the whole, favoring liberalization regardless of the circumstances and it needs to be much more self critical.

LITTLEJOHNS: This is **World Chronicle**. Our guest is John Langmore, Director of the Division for Social Policy and Development at the United Nations Department of Economic and Social Affairs. Linda Fasulo.

FASULO: Mr. Langmore, to give us a better sense and flavour of how the World Bank works are there any examples of loans that they have given or areas where they have

really excelled in effecting changes in specific countries? What do they really do right now and how should that be kept in their mandate?

LANGMORE: You would be better to ask someone from the World Bank that question but clearly, at present, they are building up their support for education and health services for example and that's enormously important as we all agreed earlier. The principal requirement for reducing poverty, which the Bank now says is its central goal, is ensuring that everyone is both literate and numerate and still 130 million people worldwide don't have access to basic education. The Bank is focussing on that really very strongly and trying to help countries ensure there are opportunities for basic education available for everyone. So that's a very good example of an evolution of policy in a very constructive way, I think.

FASULO: And how would you want to see the voting structure change within the World Bank?

LANGMORE: I think to recognize the extent to which changes in income have occurred globally and also there needs to be some recognition of the change in country size, so both those dimensions are relevant. And that would mean some reduction in the voting power of developed countries, some increase in the voting power of developing countries. Most people would accept that to some degree, even though the Managing Director of the International Monetary Fund said that he would like to see the voting power of East Asia increase. Well, that's a very logical step but it needs to be a more democratic process in the sense that there's a better reflection of global population distribution in the voting pattern I think.

LITTLEJOHNS: John, in the introduction we said that these institutions need to be overhauled before a crisis induced by globalization -- that terrible "g" word -- forces the changes required. Now why is globalization going to force these changes?

LANGMORE: I think the lesson of 1997-98 is that financial crises can come extraordinarily quickly and unexpectedly and have a direct effect on a great range of other countries through contagion. And whilst, before that, officials of the Fund would say we've got everything under control, crises are no longer possible, now they would not say that. The world financial system is too uncertain and too complicated a place to ensure that every possibility is covered. So there is a growing risk of a rapid spread of any crisis that occurs

because of the growing interdependence, and that means that the resources available to the Fund for handling crises and the regulatory framework within which that occurs needs to be constantly worked on and, to a large extent, upgraded. The Fund does not have the adequate resources for a major financial crisis.

LITTLEJOHNS: You're speaking of the International Monetary Fund?

LANGMORE: The International Monetary Fund, yes.

HOLLOWAY: There seems to be a paradox in the report. It says that developing countries are in a race to the bottom to attract investment and that in this race they will cut corners on environmental protection, that they will repress trade unions, cut corners on workers' rights, and so on. And this, I think, is one of the things that makes people scared about globalization and then, in not quite the same breath, there's another paradox. You say that the WTO, the World Trade Organization, should not try to enforce these standards. Well, are you saying that the WTO is the inappropriate organization to enforce standards or the standards shouldn't be enforced at all? And if you're saying they shouldn't enforce them ...

LANGMORE: No. Well, the WTO is always in trade and it's not appropriate for the WTO to be enforcing standards in relation to environment or labour or finance. The race to the bottom issue covers all those areas, and others. One way in which developing countries have been making it a lot more difficult for themselves in a sense is by reducing their corporate tax rates in order to make themselves more attractive to foreign investors. And now there's hardly a developing country whose corporate tax rate is more than 20 percent, yet corporate revenue collections are one of the main ways in which foreign direct investors contribute to a developing country when investment occurs. So to attempt to set minimum standards through the appropriate organization -- and there isn't an organization by the way in the tax field that could set such grade standards.

HOLLOWAY: But that's the point I was going to make. If not the WTO which part of the UN system could enforce these standards? Are new institutions required or ...

LANGMORE: Yes, they are and in this area, tax is a good example. There is no institution globally that is providing an adequate basis for cooperation between countries other than tax systems in order to enable these countries ...

LITTLEJOHNS: A lot of people might say, thank God.

LANGMORE: Well, they might. They might. But anyone who is concerned about the tax they pay – unless they are a serious tax avoider – would not say that because to the extent that large income earners are able to avoid their taxes you and I have to pay more. Therefore, to set a framework within which it's more difficult for the big tax avoiders to get away with paying little tax, is to all of our advantage so that's one reason why – and perhaps the central reason why an international taxation organization is really important. And that possibility is on the agenda of the Financing for Development meeting which will be held in Mexico in March next year. It's early days but I think an increasing number of countries are recognizing that given the extent of inter-relationship between them, it's increasingly possible for people to minimize their tax, often dishonestly, by the way they handle them in relation to tax havens in other parts of the world. And that can only be addressed in cooperation between countries and to facilitate that, not to set tax rates or introduce new taxes but simply to protect the integrity of national tax systems, some kind of an international taxation organization has really become an imperative.

FASULO: Has the time come for an international economic security council?

LANGMORE: Well, I think so, yes, and thank you for that question. I mean a good example for us necessarily is that when a financial crisis occurred in 1997 there was no political forum where that could be immediately addressed. I mean it could have been addressed in the Economic and Social Council but the Economic and Social Council still doesn't operate in that way. It was immediately addressed through the International Monetary Fund, in cooperation with the US Treasury, and various steps were taken that were very important and very valuable. But it would have been more constructive and more democratic if immediately that crisis had occurred there'd been an Economic Security Council or an upgraded ECOSOC – Economic and Social Council – which would have met and discussed the issue and talked about the framework of the response and allocated responsibility for various parts of the response. And we don't really have that opportunity at present. Many people would say that there are gaps in the institutional framework and the policy framework for managing a globalizing world and I think that that's true. And so given that the UN is the political heart of the international system at least the political dimensions of

that discussion ought to be taking place here and an Economic Security Council would be an institutional arrangement for doing it.

LITTLEJOHNS: Speaking of the existing Security Council, aside from any institution that might be developed later, why are you guys worried about the veto in the Security Council? I mean, the veto is supposed to a very valuable instrument.

LANGMORE: Because it's obviously not democratic. I mean it gives ...

LITTLEJOHNS: Well, what makes us think that the UN is democratic?

LANGMORE: Well, I don't the UN is fully democratic either. I agree with you. It's not democratic for China to have one vote and Nauru one vote. So there is absolutely clear answer to this. But is it fair that five countries – the permanent five – have an absolute veto on what happens and for all the rest of the world to be excluded from ...

LITTLEJOHNS: Well, if life were fair, John, we'd all be Rockefeller right? So I mean fairness is really not what we are discussing, is it?

LANGMORE: I hope it is because the Millennium Assembly said that social justice was one of the central principles which should operate in the world and that is at the heart of the UN tradition of values and goals. And the veto of the permanent five is inconsistent with that. Now, of course it's hard to change and of course they wouldn't want to give it up and a step of reform might be to extend the number of countries that are permanent members of the Security Council with a veto.

LITTLEJOHNS: Give them the veto as well?

LANGMORE: Some would argue. Some would argue. I'm not necessarily doing so. Some would argue that that would reduce the unfairness of four developed countries and one developing country having a veto if to that were added India, one country from Africa, one country from Latin America. But I'm not advocating that. I'm just pointing out the inconsistency of the present situation.

HOLLOWAY: One of the ideas that you suggested in the report is for a parliament, a people's assembly, modelled on the European parliament. Do you think that would make the UN more democratic and if so, how? Also I'm rather intrigued you would use the European parliament as a model because in Europe the parliament is, I think, seen as

something of a joke and people don't take it a lot seriously. It doesn't seem to have any teeth. Participation in elections very, very low when compared to national elections.

LANGMORE: Well, the European Parliament has slowly increasing influence – I don't think that's disputable – and many people would say there's still a democratic deficit in Europe. But the capacity of the parliament to have influence is growing as the resignation of all the commissioners in response to an enquiry through the parliament showed. So its influence is growing. I think what's behind the idea for a people's assembly at the UN is the recognition that the UN is representative of national governments only. Now they're representatives of their peoples but they're not representative of parliaments, necessarily, and they're certainly not representative of lots of opinion within countries. Now, there might well be scope for some kind of advisory global assembly elected broadly – goodness knows how. I think it's very difficult to define the ways of doing this but accepting that there are going to be difficulties. I don't think it's impossible and to have such an assembly, perhaps meeting for two or three weeks a year and discussing main issues that were being addressed by the UN, could contribute to expanding the range of issues and ideas that are available to the policymakers here.

LITTLEJOHNS: Mr. Langmore, that's all the time we have. Thank you for being with us on this edition of **World Chronicle**.

Our guest has been John Langmore, Director of the Division for Social Policy and Development at the United Nations Department of Economic and Social Affairs.

He was interviewed by Robert Holloway of *Agence France-Presse/AFP* and Linda Fasulo of *NBC News*.

I'm Michael Littlejohns. Thank you for joining us. We invite you to be with us for the next edition of **World Chronicle**.

ANNOUNCER: Transcripts of the programme may be obtained free of charge by sending a stamped, self-addressed envelope to **World Chronicle**, United Nations, Room S-827L, New York, N.Y., 10017.

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